IN THE

Supreme Court of the United States

October Term, 1954

No. 25

UNITED STATES OF AMERICA,
Petitioner,

vs.

EDWARD B. CALDERON,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR RESPONDENT

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OPINION BELOW

The District Court rendered no opinion. The opinion of the Court of Appeals (R. 218-219) is reported at 207 F. 2d 377.

JURISDICTION

The judgment of the Court of Appeals was entered on October 9, 1953 (R. 220). A petition for rehearing, filed on November 22, 1953, was denied on December 8, 1953 (R. 220). The petition for a writ of certiorari was filed on February 4, 1954, and was granted on June 7, 1954 (R. 223). The jurisdiction of this Court rests on 28 U. S. C., Section 1254.

QUESTIONS PRESENTED

1. Where an income tax evasion prosecution is based upon an increase in net worth, is this circumstantial evidence which must exclude every reasonable hypothesis other than that it was derived from current taxable income?

2. In an income tax evasion prosecution, must there be some independent proof of the corpus delicti before the Government may rely upon a defendant's extra-judicial admissions?

3. In an income tax evasion prosecution based on proof of unexplained increases in net worth, must the Government prove each pertinent item of the net worth statement at the starting point to a reasonable certainty?

4. May the Government use the net worth method without showing that the taxpayer's books were inadequate to clearly reflect his income, without offering his books in evidence, and without pointing to any specific income which was omitted from his books or income tax return?

5 Where the sole proof of unreported income is based upon increases in net worth alone, is that evidence from which a jury may properly find an intent to evade taxes, or must the Government offer independent evidence of willfulness?

STATUTES INVOLVED

Internal Revenue Code (1939 ed.):

Sec. 41. General Rule.

> The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal

year or calendar year, as the case may be) in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income. If the taxpayer's annual accounting period is other than a fiscal year as defined in section 48 or if the taxpayer has no annual accounting period or does not keep books, the net income shall be computed on the basis of the calendar year. (Title 26, USC 1946 ed., Sec. 41)

Sec. 145 (b). Penalties.

> * * * and any person who willfully attempts in any manner to evade or defeat any tax imposed by this chapter or the payment thereof, shall, in addition to other penalties provided by law, be guilty of a felony and, upon conviction thereof, be fined not more than $10,000, or imprisoned for not more than five years, or both, together with the costs of prosecution. (Title 26 USC 1946 ed., Sec. 145 (b))

STATEMENT

Respondent was charged with willfully attempting to evade his own and his wife's joint income tax liabilities for the years 1946, 1947, 1948 and 1949, in violation of Section 145(b) of the Internal Revenue Code (1939 ed.) (Title 26 U. S. C. 1946 ed. Sec. 145(b)) (R. 3-6). He was an operator of a small legitimate coin-machine business in Douglas, Arizona (R. 156-157, 180). He had a meager education, having gone to high school only two months, and

had started in business with two machines in 1935 (R. 153, 154). Being unfamiliar with books and records, he obtained the services of his brother's employer, a Mr. Speer, an elderly man who operated a confectionery store. Speer told respondent to get some sales books, and then proceeded to keep books for the respondent in a complete, but rather primitive way, from about 1936 to about 1943 (R. 133, 134, 157, 158). During that period, Speer made out respondent's income tax returns (R. 158).

In 1943, Speer's health failed, and respondent obtained the services of a friend, Eugene C. Verdugo, on a part-time basis to keep the books and prepare the income tax returns (R. 134, 158, 159). Verdugo, whose occupation was manager of a lumber company, did this work as a favor to respondent (R. 127, 134). Verdugo was not an accountant or tax expert; but used his knowledge of bookkeeping to do outside extra work for friends to augment his income (R. 133). He prepared the tax returns from 1943 to 1950 inclusive (R. 128-129). During the course of the investigation by the internal revenue agents, Verdugo and respondent cooperated fully with them, and turned over all of respondent's books and records (R. 87, 88, 140, 172-173).

During the war respondent had music boxes, automatic pinball machines and cigarette machines at various locations in the city of Douglas and surrounding territory (R. 156-157). He also had slot machines at the Douglas Air Base, outside of Douglas, where they were allowed (R. 161). Business was very good during the war years, but since he could not buy new equipment, he did not have to spend much money (R. 161-163).

When he began operations in 1935 he kept his money at home in a trunk (R. 157), but about 1944 or 1945 began

to use a safe (R. 163). The nature of his business required him to keep large amounts of cash and change in that safe (R. 138, 163). Although he made some deposits in banks, he built up a reserve in cash in the safe which amounted to $16,000 or $17,000 at the end of December 1945 (R. 164). During 1946 when new equipment became available, he purchased about $16,000 worth of new machines (R. 64-66, 164-165). Approximately $15,000 of these purchases represented cash outlay (R. 91). The purchases of equipment reduced the amount of cash in the safe to $3,000 or $4,000 at the end of 1949 (R. 165).

Verdugo made entries in the books from information supplied by respondent. He was given a list of locations for every month, and the amounts taken in from each location. He also had a roll of invoices and a list of checks for each month (R. 127-128). To avoid the possibility of any receipt books being lost or misplaced by respondent or his employees, Verdugo numbered them in sequence (R. 130-131).

The Government offered no direct evidence of any income received by respondent and not reported on his income tax returns. It did not offer in evidence the books and records of respondent, upon which the returns were based (R. 129), and did not contend that they were inadequate. The agent admitted the books were set up in an acceptable form. He found no mathematical errors, but in his opinion a good deal of the coin-operated machines money was not recorded in the books (R. 89). But no direct evidence was offered of any income omitted.

The Government called only five witnesses: two bank officers who identified records, Deputy Collector Webb and Special Agent Tucker of the Bureau of Internal Revenue

who conducted the investigation of respondent's income tax liability, and Mr. Verdugo (R. 31, 34, 40, 50, 127). Only Mr. Verdugo had any knowledge of respondent's business or income, and that was derived entirely from respondent. He had no independent knowledge of respondent's business (R. 129).

The only evidence offered by the Government of any income of respondent above that reported on his income tax returns was the admission of respondent in Government's Exhibit 11 (R. 106-110). For proof of understatements of income the Government relied entirely upon "increases in respondent's net worth plus non-deductible expenditures" (Br. 4). The agents had obtained respondent's signature to a formal net worth statement which they had prepared, respondent's Exhibit B (R. 50, 52, 87, 195, Br. appendix), but the Government did not offer it in evidence.

During the investigation the agents had interviewed respondent several times (R. 90, 175). On August 2, 1950 Agent Tucker, prepared Exhibit 11, and had respondent sign it (R. 106). Webb testified that the net worth statement had been prepared previously, and that after going over it with respondent, he signed it, although the agents had not asked him to do so (R. 123-124). Respondent testified that he did not understand Exhibit B, but signed it solely because his bookkeeper, Verdugo, said it was all right to do so (R. 176-177, 187). Verdugo testified that he was shown the net worth statement by the agents, but that he made no independent investigation of the figures on it, and did not know a thing about any of them. He relied entirely upon the agents as to the accuracy of the figures, and simply approved the procedure they had followed (R. 140-141).

Agent Tucker also testified that respondent relied upon Verdugo, and that the latter had stated: "I don't know about all the figures on it but it is a commonly used method of determining income and it looks all right to me" (R. 87).

For purposes of the trial respondent stipulated that Special Agent Tucker might testify as to all of the items on the net worth statement with the exception of assets designated as "cash on hand" and "cash in bank" (R. 8-9, 54). This net worth statement, Exhibit B (Br. App.) (which was used by Tucker as notes for his oral testimony) lists as "cash on hand" $500 on December 31st of each of the six years 1943 to 1948 inclusive, and $1,971.50 on December 31, 1949. On direct examination Tucker testified that respondent had told him that to the best of his recollection "he would have had $500.00 on hand on the last day of each year" (R. 59). However, when Tucker pointed out a cash deposit in the bank of $1,971.50 on January 4, 1950, and asked whether it would be possible to accumulate that much cash between January 1 and January 4, respondent accepted Tucker's suggestion that it must have been some receipts carried over from the end of the year. Tucker testified that respondent then said he had $500 in cash on hand on December 31st of every year except 1949, when he had exactly $1,971.50 (R. 59, 60).

On cross-examination Tucker admitted that what respondent actually had said was that he ordinarily carried $500 in his pocket (R. 80, 86). Over the Government's objection, respondent offered in evidence the typewritten notes (Respondent's Exhibit A) from which Tucker had been testifying, which purported to be a memorandum of his conversation with respondent (R. 81). This exhibit stated that respondent told Agent Tucker: "On January 1,

1944, he had approximately $500.00 in cash *in his pocket.* He believes that because it is his habit to carry that much money in his pocket at all times" (italics supplied) (R. 82). Agent Tucker also testified:

> "This item of cash in pocket, as I said before, is terminology. I didn't interpret he carried five hundred in his pocket at all times. It is obvious that he had more cash at times because his savings account shows he deposited one thousand or two thousand or more at a time, so it is evident he had it the day before he deposited it and probably for days or weeks before. Of course at times he had more cash than that." (R. 85)

In Exhibit 11, the affidavit of respondent prepared by the agents, the agents did not include any reference to the alleged $500.00 cash on hand or in pocket at the end of each year. The only pertinent reference to cash on hand is the statement: "Excess receipts I accumulated in my safe for short periods of time and then deposited such moneys in my savings account" (R. 107-110). Verdugo also told the agents that respondent carried plenty of cash in his safe, because of the nature of his business; he had to be making change, cashing checks and so forth, for his locations (R. 86, 138). The agents never inquired as to how much money was in the safe (R. 80, 85, 139, 176).

The Government offered no independent evidence of the item "cash on hand", but relied solely upon alleged verbal admissions of respondent. In fact, the Government made no attempt to offer any independent evidence to exclude the hypothesis that the funds respondent used to acquire the assets listed in the agents' net worth statement might have been from sources other than current business income.

No independent evidence of lack of previous savings, lack of previous or immediate inheritances to himself or wife or lack of previous resources was presented. For a beginning to the net worth statement, the Government relied entirely upon the alleged admissions of the respondent.

The admissions of respondent to the agents, particularly with reference to the item of "cash on hand" were the principal issues in the case. At the inception of the trial respondent stipulated to all items on the net worth statement except "cash on hand" and "cash in bank" (R. 8-9). Throughout the trial, respondent objected to evidence of the alleged admissions, and made appropriate motions to dismiss the indictment and to render a verdict for respondent, due to the failure of the Government to prove a case or to prove the corpus delicti by independent evidence (R. 54, 57, 62, 68, 98, 100, 107, 141, 198).

The Court of Appeals for the Ninth Circuit reversed the conviction and ordered a new trial (R. 220). The Court held that the burden of proof was on the Government as to each pertinent starting item of the net worth statement to a reasonable certainty. Since there was no independent proof of any portion of the corpus delicti, the extra-judicial written and oral statements of the respondent were not competent or admissible to establish the starting items of the net worth statements or understatement of income. The Court indicated that the admissions of the respondent as related by government agents were insufficient to establish the item of "cash on hand" anyway. Thus the prepared "net worth" statements had no valid probative value. There being no other evidence of any sort to establish "cash on hand" or to dispute the hypothesis

in favor of innocent sources of present assets, there was no evidence to support the conviction (R. 219).

SUMMARY OF ARGUMENT

1.

This is a "bare" net worth case. It represents an effort by the Government to extend the scope of prosecutions for attempted income tax evasion to new frontiers. In its zeal to enforce the revenue laws the Government is encroaching upon basic constitutional rights of citizens, and violating established principles of criminal law. It fails to recognize basic distinctions between the principles governing civil tax cases and those governing criminal cases. Apparently what the Government is now seeking is a special set of rules of criminal evidence and law to be applied to income tax prosecutions alone so that the prima facie correctness of a determination of the Commissioner of Internal Revenue will be sufficient to require a given defendant to prove his innocence. The Government here is attempting to extend to criminal cases the special rule of ordinary civil tax cases shifting the burden of proof to the taxpayer.

Some courts have expressed concern at the tendency of the Government to extend the use of the net worth method of proof. *United States* v. *Casserta*, 199 F. 2d 905, 907 (C. A. 3); *Demetree* v. *United States*, 207 F. 2d 892, 893 (C. A. 5); and *United States* v. *Riganto*, 121 F. Supp. 158, 159 (E. D. Va.) Basically, the Government's contention in the instant case is: mere proof of increased visible assets, without any evidence of their source as "income," is sufficient to make a prima facie case, and cast the burden of proving innocence on the citizen taxpayer.

2.

The net worth method is unreliable as a means of determining current taxable income. The form of statement generally compiled by the Government is not a true net worth statement from an accounting standpoint, but rather a statement of visible assets listed as cost owned by the taxpayer on a specific day, less known liabilities. The Government adds to its list of assets known expenditures during the year.

The net worth method is not an accurate means of determining current income. While a steadily increasing net worth over a period of years, computed from definitely established beginning assets, may justify an inference of income, it does not show definitely in which year. At best it yields only a rough approximation of what the income might be. *United States* v. *Riganto, supra, Thomas A. Talley* v. *Commissioner,* Docket Nos. 33140, 33141, 20 T. C. No. 101.

3.

The courts originally permitted the Government to use the net worth method *as corroboration* of direct evidence in cases involving lucrative illicit enterprises which kept no books or records. See *Gleckman* v. *United States,* 80 F. 2d 394 (C. A. 8), certiorari denied 297 U. S. 709; *Schuermann* v. *United States,* 174 F. 2d 397 (C. A. 8) certiorari denied 338 U. S. 831; *United States* v. *Johnson,* 319 U. S. 503; *Lurding* v. *United States,* 179 F. 2d 419 (C. A. 6). Permisseion to use such indirect evidence of income was justified as reinforcement of direct proof where "an elaborately concealed illegal business was involved." *United States* v. *Johnson, supra,* p. 518.

4.

As the Government has extended the use of this net worth method to prosecutions of taxpayers in legitimate businesses, the courts have established certain definite requirements of proof which the Government must meet in order to safeguard the rights of defendants under the rules governing the use of circumstantial evidence.

(a) Taxpayers have a right to have their taxes computed in accordance with the method of accounting used by them in preparing their returns, (I. R. C. Sec. 41) and since the net worth method is not a normal accounting method for determining annual income, the courts have held that the Government may use the net worth method, only where (1) no method of accounting was regularly employed by the taxpayer, or (2) the method employed did not clearly reflect his income. Where the taxpayer's books are adequate to reflect income there must be some external evidence of unrecorded income in order to use this method.

(b) The Government must show a source or sources of income to account for the increase in net worth. Such a source may be either (1) a definite source of income discovered by the Government and not reflected in the books or in the returns, or (2) income which, while reflected in the books, is recorded either incorrectly or with demonstrable omissions.

(c) In sustaining its burden of proof of unreported income the Government is required to establish the taxpayer's net worth at the beginning and end of each tax year to a reasonable degree of certainty. This imposes upon the Government the necessity of establishing an accu-

rate starting point. In order to justify the inference that an increase in visible assets resulted from current receipts, the Government must demonstrate that the assets and liabilities at the starting point are accurate, and that there were no other assets at that time. "Essential proof of no other assets is the cornerstone of the evidence of the government." *United States* v. *Fenwick*, 177 F. 2d 488, 492 (C. A. 7).

(d) After establishing an accurate starting point, the Government must then establish that any annual increases in net worth were from current taxable income. It must justify the inference that such increases came from a source of income discovered by the Government, or otherwise specifically identified, and not from non-taxable sources, such as gifts, inheritances, insurance proceeds, soldier's bonuses, etc. It cannot assume that any visible increase in net worth necessarily resulted from unreported current taxable income.

5.

There are two elements to be proven to establish the offense of attempted tax evasion (1) unreported taxable income and (2) a willful intent to evade the tax thereon. Because of the particular nature of the offense the corpus delicti encompasses the whole of it. In most criminal offenses there are two separate parts to the corpus delicti (1) that an injury occurred, such as death by homicide, and (2) that someone caused the injury. Since the failure to report taxable income is not an offense unless the failure is willful, it is not possible to prove a crime took place without establishing the guilt of the person who committed it.

6.

At the trial of this case the Government relied upon respondent's oral and written statements to internal revenue agents as the sole proof of essential elements of the offense. It tried the case on the theory that proof of annual increases in net worth were sufficient without more to establish (1) that respondent had understated his taxable income, and (2) that he willfully intended to evade the tax thereon. An agent testified that the respondent had orally admitted having only $500 cash on hand on December 31st of each of the six years 1943 to 1948, inclusive. (Respondent contends that on cross-examination the agent admitted this was not exactly correct, so that the fact of the admission is itself in question.) Another agent offered in evidence a statement signed by the respondent admitting that his income had been understated.

The Government selected December 31, 1945 as its starting point and relied upon respondent's alleged admission that he had only $500 cash on hand as sole proof of that item. It offered no proof at all with respect to the nature of respondent's business or his income and relied upon his written admission of understatement of income as sole proof that taxable income from any source was unreported. It did not produce his books and records in court, and conceded they were adequate to reflect his income. The agents disregarded the books solely on the basis that in their opinion he had omitted some income. They offered no independent proof at all of any income omitted from his books or returns. The Government offered no independent proof to establish the item cash on hand, or to refute the possibility that he did have cash on hand at the starting point which might have been used to purchase the visible assets seen

by the agents. On the contrary, the Government's own evidence supported respondent's testimony that he had purchased the assets they listed with funds accumulated in prior years.

7.

The court below ruled that it was error to receive in evidence respondent's oral and written admissions without some independent proof of the corpus delicti. The Government contends (1) that it did offer some independent proof of the corpus delicti, and (2) that the court below has broadened the rule requiring corroboration of admissions to include independent evidence of even a subsidiary fact.

Respondent disagrees with the Government's interpretation of the decision of the court below. That court properly held that the burden is on the Government to prove each item in the starting point to a reasonable certainty. The court further held that mere proof of an increase in visible assets was not proof of any material part of the offense charged, and was not independent proof of the corpus delicti. The Government's contention that proof of an increase in visible assets in a given year is sufficient proof of unreported taxable income, is an attempt to establish the corpus delicti by conjecture and innuendo. The Government wishes to be relieved of the burden of proving the item cash on hand and asks that the burden of proof be shifted to the taxpayer. In support of this contention it cites cases which relieved the Government of the necessity of proving a negative averment under certain special circumstances involving contraband or acts of a sinister nature.

Respondent contends that in a case such as this, involving prosecution of a legitimate businessman, based solely upon alleged increases in net worth, "proof of no other assets", including the opening item cash on hand is the cornerstone of the Government's case. Without proof of this element there can be no accurate starting point, and consequently no basis for determining any increase in net worth. Without proof of an increase in net worth there is nothing from which to infer any income, let alone the question of whether the income was from current non-taxable sources.

8.

A bare net worth case lacks any evidence from which a jury could properly draw the inference of an intent to evade a tax. In the instant case there was no evidence at all offered of any affirmative act of respondent which could be the basis of a finding of a willful attempt to evade a tax.

ARGUMENT

I.

THERE WERE NO ADMISSIONS TO AGENTS BY RESPONDENT OF CASH ON HAND AT THE BEGINNING OF ANY YEAR

At the outset the nature and content of respondent's alleged admissions should be made clear. The Government erroneously implies that the court below held that respondent admitted "that he had $500 in cash on hand at the starting point" (Br. 12). While the prime issue in this case is whether *any* admission may be received in evidence without

independent evidence of the corpus delicti, it would be erroneous to assume that the court below accepted the Government's contention in reaching its decision.

The Government's contention that the item cash on hand on Exhibit B was based on respondent's previous oral admission is not borne out by the record (Br. 9, 10). Respondent developed on cross-examination of the Government agents that respondent had never in fact made the statement that he had only $500 cash on hand at the beginning of each year. Respondent had no fear of the agents' testimony, and over the Government's objection demanded the notes from which agent Tucker was testifying, and offered them in evidence (Respondent's Exhibit A, R. 81). This exhibit purported to be a memorandum of an interview with respondent, prepared and signed by the agents. It stated: "On January 1, 1944 he had approximately $500.00 in cash *in his pocket*. He believes that because it is his habit to carry that much money in his pocket at all times" (italics supplied) (R. 82).

In Exhibit 11, the affidavit of respondent prepared by the agents, the agents did not include any reference to the alleged $500 cash on hand or in pocket at the end of each year. The only pertinent reference to cash on hand is the statement: "Excess receipts I accumulated in my safe for short periods of time and then deposited such moneys in my savings account" (R. 107-110). It is significant that in the only written statements referring to conversations with respondent there is no admission that he had only $500 in cash on hand at the beginning of any one year. The record is clear that respondent refuted the accuracy of the net worth figures and offered Exhibit B, not as proof of the figures thereon, or as an admission of the

figures, but as physical proof of the inaccuracies of the agents' testimony (R. 80, 86, 187-190, 195). Respondent signed Exhibit B, although he did not understand the figures, solely because Verdugo said "I don't know about all the figures on it but it is a commonly used method of determining income and it looks all right to me" (R. 87, 140-141, 176-177, 187).

The direct testimony of agent Tucker that respondent admitted having *exactly* $500 cash on hand on December 31st of each of the years 1943 to 1949, inclusive, and *exactly* $1,971.50 on December 31, 1949 is not only highly improbable, but was completely destroyed on cross-examination by his admission:

> "This item of cash in pocket, as I said before, is terminology. I didn't interpret he carried five hundred in his pocket at all times. It is obvious that he had more cash at times because his savings account shows he deposited one thousand or two thousand or more at a time, so it is evident he had it the day before he deposited it and probably for days or weeks before. Of course at times he had more cash than that." (R. 85)

Since the *only* evidence offered by the Government that respondent admitted having only $500 cash on hand on December 31st of each year was the oral testimony of agent Tucker, it is clear that the cross-examination deprived his direct testimony of any probative value. The court below did not have to determine whether there was sufficient credible evidence of this admission, since it held that even on the Government's contention, it was inadmissible for lack of some independent evidence of the corpus delicti.

The only other alleged admission of respondent was the statement typed by agent Tucker and signed by respondent that he had understated his income (Exhibit 11, R. 109). The Government contends he made a similar extra-judicial admission to Verdugo during the investigation (R. 131-132, Br. 10). Agent Webb admitted that respondent had not made any such admission in their interviews with him, and that the first time it was said was in the statement prepared by agent Tucker (R. 126). There was no independent evidence whatsoever that any receipts were omitted from the books or income tax returns. The Government relied entirely upon the alleged admissions that income was under-stated.

II.

IN A PROSECUTION FOR INCOME TAX EVASION THE CORPUS DELICTI INCLUDES EACH OF THE ESSENTIAL ELEMENTS OF THE OFFENSE.

Although the term "corpus delicti" has been used quite generally in considering the requirements of corroboration for the receipt of admissions and confessions in evidence, there has not been complete agreement as to its definition and application to various offenses.[1]

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[1]BOUVIER'S LAW DICTIONARY, Vol. 1, p. 686, defines "corpus delicti" as follows:

> "CORPUS DELICTI. The body of the offence; the essence of the crime.
>
> It is a general rule not to convict unless the corpus delicti can be established, that is, until the fact that the crime has been actually perpetrated has been first proved. Hence, on a charge of homicide, the accused should not be convicted unless the death be first distinctly proved, either by direct evidence of the fact or by inspection of the body; Best, Pres. § 201; 1 Stark. Ev. 575. See 6 C. & P. 176; 2 Hale, P. C. 290; Whart.

In most criminal offenses there are two separate parts to the corpus delicti, (1) that an injury occurred, such as death by homicide, and (2) that someone caused the injury. Proof of the first element is entirely separate from proof of the second. The guilty person could be anybody, and the prosecution's task is to connect some person with the injury. But in the offense of income tax evasion, the two elements are not separable. If a tax is due, the only person who can be guilty of attempting to evade it is the person who

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Cr. Ev. § 324. Instances have occurred of a person being convicted of having killed another, who, after the supposed criminal has been put to death for the supposed offence, has made his appearance alive. The wisdom of the rule is apparent; but it has been questioned whether, in extreme cases, it may not be competent to prove the basis of the corpus delicti by presumptive evidence; 3 Benth. Jud. Ev. 234; Wills, Cir. Ev. 105; Best, Pres. § 204; 3 Greenl. Ev. 30. In cases of felonious homicide, the corpus delicti consists of two fundamental and necessary facts: first, the death; and secondly, the existence of criminal agency as its cause; *Pitts* v. *State*, 43 Miss. 472. A like analysis would apply in the case of any other crime."

WIGMORE ON EVIDENCE, 3rd Ed., Vol. VII, Sec. 2072 states:

"§ 2072. (3) Definition of 'Corpus Delicti.' The meaning of the phrase 'corpus delicti' has been the subject of much loose judicial comment, and an apparent sanction has often been given to an unjustifiably broad meaning. It is clear that an analysis of every crime, with reference to this element of it, reveals three component parts, first, the occurrence of the specific kind of injury or loss (as, in homicide, a person deceased; in arson, a house burnt; in larceny, property missing); secondly, somebody's criminality (in contrast, e.g. to accident) as the source of the loss,—these two together involving the commission of a crime by somebody; and, thirdly, the accused's identity as the doer of this crime.

(1) Now, the term 'corpus delicti' seems in its orthodox sense to signify merely the first of these elements, namely, the fact of the specific loss or injury sustained:

* * *

This, too, is 'a priori' the more natural meaning; for the contrast between the first and the other elements is what is emphasized by the rule; i.e. it warns us to be cautious in convicting,

owes it.[2] The offense consists of two main elements: (1) a failure to report taxable income, and (2) a willful attempt to evade the tax thereon. Since the failure to report taxable income is not an offense unless the failure is willful, it is not possible to prove a crime took place without establishing the guilt of the specific person who committed it. In other crimes, such as murder or larceny, proof that a crime was committed is independent of proof of identity of the guilty party. Thus, because of the particular nature of the offense of attempted income tax evasion, the corpus delicti encompasses the whole of the offense. Up to this point respondent is in agreement with the Government (Br. 28). He disagrees with the Government's illogical attempt to change the element of *unreported income* to merely *increased assets* in the corpus delicti. The Government assumes it can, in a prosecution based *solely* on the net worth theory of circumstantial evidence, eliminate one of the cornerstones essential in building the net worth structure. See *United States* v. *Fenwick*, 177 F. 2d 488, 492 (C. A. 7). Without correct assets as a starting point, it is impossible to create a "net worth" statement which indicates taxable *income*. The Government appreciates this truth, and therefore attempts to change the first element of the crime to: "(1) A failure to report an apparent gain in assets, from any source, taxable or not."

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since it may subsequently appear that no one has sustained any loss at all; for example, a man has disappeared, but perhaps he may later reappear alive. To find that he is in truth dead, yet not by criminal violence—i.e. to find the second element lacking, is not the discovery against which the rule is designed to warn and protect us.

(2) But by most judges the term is made to include the second element also, i.e. somebody's criminality:"

* * *

[2]While others may be guilty of aiding and abetting, there can be no offense under Sec. 145(b) unless the taxpayer is also guilty.

III.

WHERE THE NET WORTH METHOD IS USED TO ESTABLISH INCOME TAX EVASION, THE GOVERNMENT MUST PROVE AS ESSENTIAL ELEMENTS (1) THAT THE TAXPAYER'S BOOKS AND RECORDS WERE NOT AVAILABLE OR WERE INADEQUATE TO DETERMINE INCOME, (2) A SOURCE OF INCOME TO ACCOUNT FOR THE INCREASE IN NET WORTH, (3) A FIXED STARTING POINT AT WHICH THE TAXPAYER'S FINANCIAL CONDITION IS AFFIRMATIVELY ESTABLISHED WITH SOME DEFINITENESS, AND (4) THAT INCREASES IN NET WORTH WERE NOT FROM NON-TAXABLE INCOME OR RECEIPTS.

In order to discuss the narrow issue of whether proof of the element of cash on hand is essential to a determination of income by the net worth method, it is first necessary to consider what are the essential elements of the offense of attempted tax evasion. The first element of the offense which the Government must prove is that there is a deficiency in tax, and that an additional tax is due for a particular year. A tax return is required for each year, and a willful attempt to evade the tax for each year is a separate offense. *United States* v. *Johnson,* 127 F. 2d 111, 119 (C. A. 7) Affirmed 319 U. S. 503.

The first task of the Government, therefore, is to prove the net taxable income.[3] Net income may be established by direct or indirect proof.[4] Where the direct proof method

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[3]While the Government is not required to prove the exact amount of unreported income (*United States* v. *Johnson,* 319 U. S. 503, 517), it is required to prove failure to report a substantial taxable income. *United States* v. *Schenck,* 126 F. 2d 702, 704 (C. A. 2); *United States* v. *Glazer,* 110 F. Supp. 558, 562 (E. D. Mo.)

[4]See discussion by ROTHWACKS "Indirect Proof of Income" in Symposium on Procedure in Tax Fraud Cases, American Bar Association, published by Matthew Bender & Company, 1951, p. 51 et seq.

is used, the Government offers evidence of specific income not reported, or specific false deductions claimed. There the principal issue is the intent of the taxpayer. Where direct proof is not available the courts have permitted the use of three methods of proving income indirectly by circumstantial evidence, (1) bank deposits, (2) net worth increases, (3) expenditures.[5]

Where the Government has offered substantial proof that a taxpayer had a specific source of taxable income, not disclosed upon his return, and is unable to prove by direct evidence the amount of such income, use of the net worth theory has been permitted to enable it to attempt to show by circumstantial evidence that the taxpayer had substantial unreported income. Also, where the Government has offered substantial proof of specific omissions of income from the same source as is disclosed on the return but has been unable to establish the amount, the net worth theory has been permitted. The degree to which use of this theory is permitted depends to a considerable extent upon the evidence of the taxpayer's compliance with the internal revenue laws.

1. Unreliability of Net Worth Method As Proof of Income.

The courts originally permitted the Government to use the net worth method as corroboration of direct evidence

[5]The increase in numbers of cases based upon indirect proof of income has produced several discussions of court decisions involving this method of proof: Avakian, "The Net Worth Method of Establishing Fraud," *Proceedings of New York University Eleventh Annual Institute on Federal Taxation*, pp. 707-737; Rothwacks, "Indirect Proof of Income", *supra*, pp. 47-88; Balter, *Fraud Under Federal Tax Law* (2d Ed.), pp. 313-321, 415-417; Lipton, "Recent Civil Fraud Cases—Problems of Burden of Proof," TAXES, February 1953 p. 110; Webster, "Section 145 (b) and Prior Accumulated Funds," TAXES, November, 1950, p. 1065; and Burns and Rachlin, "How to Defend Net Worth Cases," TAXES, July 4, 1954, p. 537.

in cases involving lucrative illicit enterprises which kept no books or records. See *Gleckman v. United States,* 80 F. 2d 394 (C.A. 8), certiorari denied 297 U. S. 709; *Schuermann v. United States,* 174 F. 2d 397 (C. A. 8) certiorari denied 338 U. S. 831; *United States v. Johnson,* 319 U. S. 503; *Lurding v. United States,* 179 F. 2d 419 (C. A. 6).[6] The Government has gradually been extending the use of the net worth method and using less and less direct evidence. The unreliability of this indirect method of proof has been recognized by some courts.

The kind of net worth statement used by the Government is not a true "net worth" statement from the accounting standpoint, but rather a statement of visible assets, listed at cost, owned by the taxpayer on a specific day, less known liabilities. The Government adds to its list of assets known expenditures during the year, such as insurance premiums, contributions, taxes paid, and an estimate for living expenses. The statement should deduct any non-taxable income, non-taxable portion of capital gains, inheritances, gifts, etc. It cannot list assets at present value, since neither depreciation nor appreciation in value involve expenditure of funds of a taxpayer.

The net worth method may sound like a fairly definite method for ascertaining increases in income, but it has many complications. Its first weakness is that it is not an accurate method of reflecting annual income. Over a period of

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[6]As Judge Yankwich recently stated in *United States v. Wilbur I. Clark*, So. Dist. Cal. decided August 4, 1954, unofficially reported 1954 CCH para. 9546:

> "A study of the cases will reveal the fact that the use of this method was sanctioned because it related to illegal activities by persons, who, because of the nature of their business, could not and would not keep books adequately reflecting their income."

several years, a steadily increasing net worth may justify an inference of income, but it equally justifies an inference of expended cash or conversion of previously held assets. The Government rarely has the complete proof necessary for an accurate statement, and usually relies upon assumptions and incomplete proof. For example, if a taxpayer is known to have owned $100,000 in securities on January 1 and not on December 31 of the same year, the Government cannot know whether his net worth decreased without ascertaining what happened to the proceeds. If the taxpayer sold the securities for $200,000, kept the entire $200,000 in a vault until the following year and then purchased $200,000 worth of new securities, the Government would erroneously assume this reflected at least $100,000 of new income in the year of purchase. It might correctly assume the amount of gain, but place it in the wrong year.

The Court of Appeals for the Fifth Circuit has expressed the growing concern of the courts at the Government's extension of the net worth method. In *Demetree* v. *United States*, 207 F. 2d 892, 893, the Fifth Circuit said:

> "This is another of the growing list of criminal cases in which the government, having no or little direct evidence of defendant's guilt to offer and endeavoring to prove it by circumstantial evidence, attempts to do so by what may be called the net worth and expenditures method of proof. In this attempt, unless the greatest care is taken by the district judge to prevent it, there is danger of the case being tried on a theory which, keeping to the ear the promise that a defendant is presumed innocent until his guilt is established beyond a reasonable doubt, breaks it to the hope by allowing a series of theoretical estimates and computations as to defendant's income to take the place of proof of it."

Chief Judge Hutcheson of the Eastern District of Virginia recently stated in *United States* v. *Riganto,* 121 F. Supp. 158, 159 (E. D. Va.):

> ". . . In the last few years I have observed with interest a change that has taken place in the nature of proof offered to support the charge of the prosecution in many of these cases charging tax fraud. This change has caused me some concern by what appears to be a preference to introduce proof to show understatement of income and fraudulent intent by methods other than by direct evidence. Of course, it is necessary in some cases that the Government proceed by indirect methods. This evidence consists of proof undertaking to show income of the taxpayer computed upon what is referred to as the net worth increase or bank deposits and expenditures methods or a combination of both. The latter is employed here. Basing my observation upon a number of cases during the past few years, it would seem that the use of one or both of these methods has been employed through preference at times when direct evidence is available."

In civil cases the Tax Court has also questioned the reliability of the net worth method as a means of determining income. In *Thomas A. Talley* v. *Commissioner,* Docket Nos. 33,140 and 33,141 20 T. C. No. 101, the Tax Court said:

> "The limitations of the increase in net worth method are well known. Often it results in an inaccurate statement of income or the placing of income in the wrong year and, at best, it yields only an approximation."

2. Adequacy of Books and Records.

Where a taxpayer has kept regular books and records, and has filed required returns, the Commissioner is required by law in the first instance to compute his tax in accordance with the method of accounting adopted by the taxpayer. The only authority the courts have cited for the use of the net worth method in either civil or criminal cases is I. R. C. Section 41 (1939 ed.).[7] This section authorized the Com-

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[7] *Jelaza* v. *United States*, 179 F. 2d 202 (C. A. 4); *Lurding* v. *United States*, 179 F. 2d 419 (C. A. 6); *Buttermore* v. *United States*, 180 F. 2d 853 (C. A. 6); *Pollock* v. *United States*, 202 F. 2d 281 (C. A. 5), certiorari denied 345 U. S. 993 (1953); *Remner* v. *United States*, 205 F. 2d 277 (C. A. 9), remanded for rehearing, 347 U. S. 227; *United States* v. *Casserta*, 199 F. 2d 905 (C. A. 3); *James Q. Whittemore* v. *Commissioner*, CCH Dec. 16, 700 (M), 7 TCM 845; *Ameen Jacob* v. *Commissioner*, CCH Dec. 17, 664 (M), 9 TCM 415; *Murray Glackman* v. *Commissioner*, CCH Dec. 18, 692 (M), 10 TCM 1132; *Thomas A. Talley* v. *Commissioner*, CCH Dec. 19, 778, 20 TC, No. 101; *Booker W. Evans* v. *Commissioner*, CCH Dec. 20, 065 (M), 12 TCM 1470; Rothwacks, article cited at footnote 4, at p. 52.

Thus the Court of Appeals for the Ninth Circuit, in *Remmer* v. *United States, supra* p. 280, 286, stated expressly that:

> "The net worth method of computing income may be used only where a taxpayer does not keep books or such books are inadequate in that they do not clearly reflect income."

In *Sasser* v. *United States*, 208 F. 2d 535, 537 (C. A. 5) the court stated:

> ". . . The net worth method of reconstructing taxable income in cases where the taxpayer has no records from which his actual income may be computed is a hybrid method of determining income based upon the cost of assets owned by the taxpayer at the beginning and at the end of each taxable period."

In *United States* v. *Williams*, 208 F. 2d 437, 438 (C. A. 3), the court stated:

> ". . . The defendant contends that his is not a proper case for the application of the net worth formula for proving tax evasion. In this he is wrong. The statute [I. R. C. § 41] provides that if the taxpayer has no regular method of accounting 'the computation shall be made in accordance with such method as

missioner to use a method different from the taxpayer's only where (1) no method of accounting has been regularly employed or (2) the method employed does not clearly reflect the income. Whether the net worth method be considered as a "method of accounting" or a "method of reconstruction of income" is immaterial, as Section 41 provides that the net income of a taxpayer "shall be computed" in accordance with the method of accounting regularly employed by him in keeping his books.[8]

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in the opinion of the Commissioner does clearly reflect the income'."

In *Bell* v. *United States*, 185 F. 2d 302, 308 (C. A. 4), certiorari denied 340 U. S. 930, the court stated:

> ". . . An estimate of the taxpayer's net worth as the means of determining his income is resorted to in the absence of accurate records which it is his duty under the statute to make and to preserve . . ."

In *Gariepy* v. *United States*, 189 F. 2d 459, 461, (C. A. 6), it was stated:

> ". . . When investigation was begun by agents of the Treasury, they were unable to find adequate records disclosing receipts of income by the appellant. The investigators then undertook to establish his income by the so-called 'net worth' method."

It is interesting to note that in *United States* v. *Friedberg*, D. C. Ohio, unofficially reported 53-2 USTC, Par. 9631, affirmed 207 F. 2d 777 (C. A. 6), certiorari granted 347 U. S. 1006, No. 18 this Term, the trial court instructed the jury as follows:

> "In this case the government is trying to establish an additional tax owing by a method known as the net worth method, which method is authorized where the bookkeeping methods of the defendant do not clearly reflect the income of the defendant. If you find that the taxpayer's bookkeeping methods do clearly reflect his income, then the government has no right to use the so called net worth method and your verdict must be for the defendant in this case as to all counts of the indictment."

[8]It has recently been pointed out to this Court that the true tax liability is such a controversial question that an official determination of the Commissioner that a tax is due should be a prerequisite to a charge of an attempt to evade a tax. (Brief of Petitioner, *Remmer* v. *United States*, *supra*, p. 23). It was further argued that use of the net worth method in determining taxable income requires a finding

The use of the net worth method in civil tax fraud cases has been discussed many times in the Tax Court. The limitations upon its use were stated clearly in *Thomas A. Talley* v. *Commissioner*, supra:

> "The ordinary method of computing taxable income in accordance with the general pattern of the Code is to subtract allowable deductions from a taxpayer's gross income. The increase in net worth method is, of course, not in accord with this statutory pattern and is permitted by virtue of section 41, I. R. C., only in unusual circumstances, none of which is present here.
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> "Section 41 provides that 'net income shall be computed . . . in accordance with the method of accounting regularly employed in keeping the books' of the taxpayer. The Commissioner's authority under section 41 to compute the income 'in accordance with such method as in the opinion of the Commissioner does clearly reflect the income' exists only if no method of accounting has been regularly employed in keeping the books of the taxpayer, or 'if the method employed does not clearly reflect the income'. See Regulations 111, sections 29.41-1 and 29.41-2."

Where books are adequate to reflect income there must be some external evidence of unrecorded income, in order to use this method. There is no prescribed detail as to just what books or how many must be kept.[9] The books must be produced in court, so that the court may determine their adequacy. Here none of the respondent's books or records

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by the Commissioner that the taxpayer's books and records were inadequate under Section 41, and that so important a decision is not left to a subordinate agent, or to the prosecutor alone (id. p. 23-26). While these points were not specifically raised in the instant case, they are issues which are present in every tax evasion case.

[9] *Bechelli* v. *Hofferbert*, 111 F. Supp. 631, 632 (D. C. Md.); *Ameen Jacob* v. *Commissioner*, *supra*, cited at footnote 7.

was produced in court, and the Government made no claim that they were inadequate. Agent Tucker claimed the books were adequate, but "there were lots of things left out" (R. 89). However, the Government offered no proof of any income left out, other than the speculative inference it asked be drawn from the alleged increase in net worth.

3. Source of Income.

The second element of the offense in a net worth case is proof of a source or sources of income to account for the increase in net worth. The income tax law does not apply to all assets received by a taxpayer during a tax year. For example, gifts may be in the form of cash or other assets, but such assets are not subject to the income tax law. There are other categories of receipts and assets which do not constitute taxable income, such as interest on tax-exempt bonds, inheritances, non-taxable portion of capital gains, recoveries in lawsuits, proceeds of insurance, soldier's bonus, etc.

A "possible" source of income must be either (1) a definite source of income not reflected in the books or on the return or (2) income which, while reflected in the books, is recorded either incorrectly or with demonstrable omissions. The Government must show some connection between a definite source of income and the increase in net worth.

In some cases the Government has proved a specific source of income by showing that the defendants were wholly or partially engaged in gambling activities, and that they kept incomplete books and records, or no records at all[10]. In

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[10] *Schuermann* v. *United States, supra; United States* v. *Johnson, supra; United States* v. *Potson*, 171 F. 2d 495 (C. A. 7); *United States* v. *Vassallo*, 181 F. 2d 1006 (C. A. 3); *Lurding* v. *United States, supra; United States* v. *Skidmore*, 123 F. 2d 604 (C. A. 7), cert. den. 315 U. S. 800.

other cases there was specific evidence of a source, accompanied by acts of concealment or deception which justified the inference.[11]

It is clear that the mere increase in assets or net worth does not justify the assumption that the increase is from taxable income. At least in a criminal case, if not also in a civil case, it is just as reasonable to assume the increase was from non-taxable sources.

In United States v. Smith, 206 F. 2d 905, 911 (C.A. 3), the court stated:

> ". . . We think it part of the Government's prima facie case to establish, at least, that what it charges against defendant is income for the year involved. It has not established its prima facie case by showing that defendant has some money and then asking the jury to infer that that money is 'income' for the year involved."

4. Starting Point.

When the Government finds resort to the net worth method necessary because it has discovered a taxpayer has specific unreported income, and his books and records were not adequate to enable it to determine his correct income, it has the difficult task of computing his net worth at the beginning and end of each tax year under investigation. It is difficult because taxpayers are not required by the revenue laws or regulations to keep such records As the Government usually goes back many years to find a starting point, evidence is not always available to establish with accuracy

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[11] *Bell* v. *United States*, 185 F. 2d 302 (C. A. 4), certiorari denied 340 U. S. 930; *Gendleman* v. *United States*, 191 F. 2d 993 (C. A. 9); *Davena* v. *United States*, 198 F. 2d 230 (C. A. 9), certiorari denied 344 U. S. 878; *Mitchell* v. *United States*, 208 F. 2d 854 (C. A. 8).

the correct assets and liabilities of a taxpayer at any given time. Even when properly established, a net worth statement is still only circumstantial evidence.

Since the Government *has chosen* to ascertain and compute the taxpayer's assets, the burden is upon it to do so to a reasonable degree of certainty. It cannot assume that whatever assets a revenue agent discovers represent all of taxpayer's assets. The net worth starting point must be accurately established, otherwise assets acquired or expenditures made during the tax years involved may be attributed to other funds or assets which were acquired prior to the starting point and not listed by the agent. The Government's problem was stated by the Court of Appeals for the Fifth Circuit in *Ford* v. *United States*, 210 F. 2d 313, 315 as follows:

> " . . . One of the most difficult matters of proof in such cases is to establish a satisfactory starting point at the beginning of the first of the tax periods included in the indictment, that is as applied to the present case, to negative the existence on January 1, 1945, of resources available to the defendant and his wife from which the excessive expenditures might have come. The Government then has the further burden in such cases of proving that there were no gifts, devises, or other non-taxable income which could have been used for the expenditures, and of proving large cash expenditures within each of the tax years considerably exceeding the taxpayer's accumulated cash resources plus reported income and which expenditures could not be otherwise accounted for than by finding that the taxpayer had received more taxable income than had been reported, and had willfully and knowingly filed or caused to be filed a false and fraudulent income tax return."

The burden which the Government must sustain in proving the starting point in a net worth case was set forth in the charge of the District Court in *United States* v. *David Friedberg,* D. C. Ohio, unofficially reported 53-2 USTC, Par. 9631 affirmed 207 F. 2d 777, (C. A. 6) certiorari granted 347 U. S. 1006, No. 18, this Term, where the court said:

> "*A clear, concise and reasonably accurate determination of the net worth of the taxpayer at the start of of the taxable period,* a source of income during the period, and an increased net worth at the end of the period which increase exceeds reported income, and established personal expenditures during the period, *are necessary circumstances which must be proved beyond a reasonable doubt before the element of additional tax owing may be established by the net worth method.*" (italics supplied)

In *United States* v. *Fenwick, supra,* a conviction was reversed because the Government failed to exclude the availability of cash on hand from certain possible sources at the beginning date of the net worth computation. The court stated, p. 492;

> "Remembering that the Government has the burden of proof in a criminal case, that the burden never shifts to defendant, that circumstantial evidence must be of such character as to exclude every reasonable hypothesis except that of guilt, it necessarily follows that, when the Government relies upon circumstances of increased net worth and expenditures in excess of reported income to establish income tax evasion, the basic net worth must be established. The defendant is not compelled to take the witness stand; he is not compelled to make proof that he is innocent, but he must be proved guilty by the evidence

> beyond all reasonable doubt, and where there is uncertainty as to whether all the assets of defendant are included in the Government's computation of net worth, it follows that its computations can not be relied on. *Essential proof of no other assets is the cornerstone of the evidence of the government; that cornerstone being faulty, the whole edifice is so weakened as to be undependable as proof of guilt beyond all reasonable doubt.*" (italics supplied)

A similar holding was made in *Bryan* v. *United States,* 175 F. 2d 223 (C. A. 5), affirmed on other grounds 338 U. S. 552, in which a conviction was reversed on the ground that a prima facie case on the net worth expenditure basis had not been made out, since the Government's proof did not exclude the hypothesis that the funds used in making some of the expenditures might have been from sources other than current business income.

5. Current Taxable Income.

Where the Government succeeds in establishing an accurate net worth starting point, it must then prove that the annual increases in net worth were from *current taxable* income. It must justify the inference that such increases came from a source of income discovered by the Government, and not from non-taxable sources, such as gifts, inheritances, insurance proceeds, soldier's bonus, etc. It cannot simply *assume* that any *visible* increase in net worth necessarily resulted from unreported *current* taxable income.

As the Court of Appeals for the Ninth Circuit said in *Remmer* v. *United States,* 205 F. 2d 277, judgment vacated and remanded, 347 U. S. 227, at p. 280:

> "The Government's case is based upon the net worth method, the underlying theory of which is that

> where a person's net worth at the end of a particular year is greater than his net worth at the beginning of that year, and such increment is not attributable to gifts, devises, loans, or other non-income sources, an inference may be drawn that the increase in net worth represents income to the taxpayer."

The same Court said in *Olender* v. *United States*, 210 F. 2d 795, 798 (C. A. 9):

> ". . . This method of proof requires the government to show the net worth of the taxpayer as of the beginning and the end of the taxable year and the non-deductible expenditures made by him that year. If the increase in his net worth plus his non-deductible expenditures exceed his reported income for the year, *and such excess is not attributable to gifts, devises, loans or other non-taxable receipts*, then the conclusion may be drawn that the taxpayer realized income which he failed to report . . ." (italics supplied)

The Court of Appeals for the Third Circuit said in *United States* v. *Casserta*, 199 F. 2d 905, 907:

> ". . . Of course it is necessary, so far as possible, *to negative non-taxable receipts by the taxpayer* during the period in question. The cases show, however, a rather surprising rule that when the discrepancy between increased net worth and reported income is shown, the burden of explanation shifts to the taxpayer, at the same time repeating the usual criminal law rule that the burden throughout a criminal case is upon the prosecution. We do not, however, get into this particular ramification in the case under discussion, for the prosecutor offered proof negativing receipts for non-taxable sources such as gifts, inheritances and so on." (italics supplied)

IV.

IN NET WORTH CASES CASH ON HAND IS AN ESSENTIAL ELEMENT WHICH THE GOVERNMENT MUST PROVE TO A REASONABLE CERTAINTY.

The entire basis of the Government's argument is that the amount of cash on hand at the starting point is not an element of the corpus delicti of attempted tax evasion, and, therefore, the Government is not required to prove it at all (Br. 13, 28). Respondent agrees that the elements of the offense are (1) unreported taxable income and (2) willful intent to evade that tax. He disagrees with the Government's contention that net income can be established under the net worth theory without proving each pertinent starting item to a reasonable certainty. The amount of cash on hand is a necessary element of proof, although not an element of the crime itself. Failure of the Government to establish cash on hand destroys the net worth theory for the establishment of unreported taxable income, and results in a complete failure of proof in the Government's case.

The Government contends that the amount of cash on hand at the starting point is not "uniformly necessary to prove that the offense has been committed—i.e., to prove the corpus delicti" (Br. 14, 28). It cites no authority for its statement. The very next sentence in its brief shows its fallacy (Br. 28). It concedes that the amounts of cash in the taxpayer's hands at the beginning and end of the year are relevant in proving an increase in net worth, which is in turn relevant to the ultimate fact of understatement of net income. This is equivalent to admitting that proof of cash on hand is a *necessary element of proof* in the instant case.

This is a *bare* net worth case, and the only evidence of additional income offered by the Government was the alleged increase in net worth. It was required to prove to a reasonable certainty *all* of the respondent's assets and liabilities at the beginning and end of each tax year under indictment.

The Government has shifted from the position it took in its petition asking for a writ of certiorari. There it said "The use of the net worth method of proof * * * depends upon the establishment of a starting point, at the beginning of the tax period involved, at which all of the defendant's known assets are computed. *An essential item of such computation is, of course, the amount of cash which the defendant had on hand at the time.* Ordinarily, this amount rests within the private knowledge of the defendant, and any effort by the Government to prove the exact amount involves inherent difficulty" (italics supplied) (Pet. 6-7).

Why did the Government contend that the decision below was "a substantial obstacle to the effective enforcement of the provisions of the internal revenue laws proscribing fraudulent tax evasion" (Pet. 7) unless the Government at that time felt it had the burden of proving cash on hand? If cash on hand is not an essential element of net worth which must be proven in order to make the assumption that any increase is current taxable income, it is of no importance to the Government whether or not the taxpayer makes any admissions.

The Government's argument has a void with respect to just where the asset "cash on hand" fits into a net worth computation. On the one hand, it contends that cash on hand is not an element of the offense, and really is of no significance (Br. 13, 19, 28), but on the other hand it strongly urges that the alleged admission by respondent of only $500 cash on hand clinches its case (Br. 16, 37).

The net worth can be determined only by computing *all* of the assets and liabilities of a taxpayer at the beginning and end of the tax year. Until the Government can demonstrate to a reasonable degree of certainty that it has listed all of the assets and liabilities, there is no basis for determining whether there has been an increase or decrease in net worth. The net worth statement cannot be considered complete just because a revenue agent contends it lists all the assets he could "find". The proof must show that the nature of his investigation was so thorough as to justify the reasonable inference that there could be no other assets.

Since the Government contends that any increase in net worth at the end of a year over net worth at the beginning of a year is due to unreported taxable income, it must not only show a definite possible source of such alleged income, but has the burden of proving the increase was not from non-taxable sources. It is just as reasonable to infer that visible increases in net worth were from gifts, inheritances or non-taxable income, as from unidentified taxable income.

Aside from non-taxable receipts during a particular tax year, it is normal and usual for every taxpayer to have cash and securities either on hand or in a safe. Accordingly, the net worth statement cannot be complete without reflecting the amount of cash, securities or other assets on hand or in a safe at the beginning of the tax period.

It is therefore essential that the Government establish to a reasonable degree of certainty that a taxpayer had no other assets on hand than those shown on its computation at the beginning of the tax period. The Government cannot reach the point of determining the net worth, until it has established to a reasonable degree of certainty either the amount of cash on hand, or the lack of sufficient cash

on hand to account for the demonstrated increase in visible assets during the tax year, not attributable to other non-taxable sources, such as gifts.

Since the item of cash on hand must be proven in order to establish net worth, it follows that where the Government bases its allegation of unreported taxable income *solely* upon an increase in net worth, the item cash on hand is an essential element of proof of unreported net income. The Government itself contends that unreported net income is one of the elements of the corpus delicti.

The weakness of the Government's argument is apparent when it is recognized that to prove one of the elements of the offense—unreported taxable income—by circumstantial evidence, it must build one stone upon another and request that inferences be drawn which must be reasonable. These building stones are (1) an accurate list of assets and liabilities at the starting point, (2) an accurate list of assets and liabilities at the end of the period which clearly establishes an increase in net worth, and (3) that such increase was not due to current non-taxable receipts. The Government contends that by merely showing *a list of assets* at the end of the tax year which is greater than a list of assets it showed at the beginning, it has proven the receipt of taxable income, and has shown "independent" proof of the corpus delicti (Br. 15). The court below correctly pointed out that "Absent such a starting item as, say, cash on hand, the remainder of the statement proves nothing" (R. 218). Where the Government fails to establish to a reasonable certainty *each* pertinent starting item of the net worth statement, including cash on hand, securities in safe, and all other assets, it has not proven the very first step on the way toward proving an offense. Cash on hand, there-

fore, is an essential element of proof to establish net worth, which in turn is the basis for determining taxable income, and unreported taxable income is an element of the corpus delicti. There can be no building without a cornerstone, and there is no chain where a link is missing.

To argue as the Government does, that cash on hand is not an element of the offense of tax evasion, is merely a play on words (Br. 28). In the instant case, based solely on net worth, cash on hand *was* an essential element of the offense. In this respect, the Government disagrees with the testimony of its agent, cited by the court below. The agent testified that "if the Cash on Hand item as it appears in your Net Worth Statement is in error then the whole thing is in error." * * * "The total taxes, the total amounts Mr. Calderon is to be charged with would be wrong all the way through." (R. 79, 219)

The reason the Government now will not admit that cash on hand is a necessary element of proof to give probative value to a net worth statement is clearly stated in the Government's Petition for Rehearing, filed in the Court below (Pet. Br. for Rehearing p. 9) where it made the direct assertion:

> "In short, visible increases in a man's wealth, beyond his reported income, clearly has probative force even though the Government presents no evidence to preclude the existance of an accumulation of cash at the starting point."

This same contention, though not clearly expressed is the sole basis for the Government's brief in this case. Perhaps the Government cannot now be expected to admit the fundamental facts of accounting theory which require a

definite asset starting point for a net worth statement. It will even less admit that proof of cash on hand is necessary to meet the reasonable requirements of the circumstantial evidence rule.

In the same Petition for Rehearing below it contended, p. 5: "* * * the item of cash on hand * * * must almost of necessity be established in many instances by the admissions of the taxpayer. * * * This Court's ruling would put an almost insuperable burden of proof on the Government by denying reliance on the exclusive source of accurate proof, i. e., the defendant's admissions."

In its petition for a writ of certiorari the Government contended "that the existence and amount of cash on hand are peculiarly within the knowledge of the defendant, and that *his failure* to present such evidence should not overcome an otherwise convincing showing of understatement of income," and cited cases (italics supplied) (Pet. 9, 10).

But inherent in the Government's argument is the contention, previously made openly, but now concealed behind other arguments, that the burden of proving cash on hand should be on the taxpayer. It states that in net worth cases defendants usually contend they had a hidden cache, and that the Government should not be required to prove a negative averment (Br. 36, 37).

This insistence that the exclusive source of proof is the taxpayer's admissions is tantamount to contending a defendant should be forced to incriminate himself. The reference to cases with respect to proof of a negative averment is further indication of the Government's position (Br. 37). The cases cited are not relevant to income tax prosecutions. *Rossi* v. *United States*, 289 U. S. 89 held that the Government was not required to prove a still was unregistered,

where it was unlawful to possess one, and the defendant could have easily shown a bond if he had one. *United States* v. *Fleischman*, 339 U. S. 349, dealt with failure to obey a lawfully issued subpoena. *Casey* v. *United States*, 276 U. S. 413, and *Yee Hem* v. *United States*, 268 U. S. 178, dealt with narcotics. The principle of all these cases is summed up in *Morrison* v. *California*, 291 U. S. 82, 90, where this Court said: "For a transfer of the burden, experience must teach that the evidence held to be inculpatory has at least a sinister significance * * * ."

In answer to the Government's contention that "the item of cash * * * must of necessity be established by the admissions of the taxpayer" respondent cites the decision of this Court in *Tot* v. *United States*, 319 U. S. 463, 469-470:

> "Nor can the fact that the defendant has the better means of information, standing alone, justify the creation of such a presumption. In every criminal case the defendant has at least an equal familiarity with the facts and in most a greater familiarity with them than the prosecution. It might, therefore, be argued that to place upon all defendants in criminal cases the burden of going forward with the evidence would be proper. But the argument proves too much. If it were sound, the legislature might validly command that the finding of an indictment, or mere proof of the identity of the accused, should create a presumption of the existence of all the facts essential to guilt. This is not permissible.
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> * * *
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> ". . . It would, therefore, be a convenience to the Government to rely upon the presumption and cast on the defendants the burden of coming forward with evidence to rebut it. But, as we have shown, it is not permissible thus to shift the burden by

> arbitrarily making one fact, which has no relevance to guilt of the offense, the occasion of casting on the defendant the obligation of exculpation."

The negative averment cases cited above are limited to special circumstances and their principle is not applicable to all the taxpayers in the country. Almost every adult in the country has some income tax liability, and there is nothing sinister or in the nature of contraband in having cash on hand.

The argument that the Government should not be required to prove cash on hand implies that this is the only kind of asset which is difficult to find. But any taxpayer may have many assets which a revenue agent can not readily find, such as cash, securities, precious stones, coins, stamps, etc. or even large assets. If he converts any asset into cash, without realizing a gain or loss, the conversion is not a transaction which must be reported on his income tax returns. Any cash so realized could be used to acquire other assets which the revenue agents may find. If the Government is not to be permitted to set up *any* list of assets a revenue agent chooses to prepare, and call it a "net worth" statement it must be required to prove to a reasonable degree of certainty that it has accounted for *all* of a taxpayer's assets, including cash on hand (See *Kirsch* v. *U. S.*, 174 F. 2d 595 (C. A. 8)).

It is quite a normal human experience to save cash, either at home or in safe deposit boxes. The Government is so ready to assume that any increase in visible assets ***must*** have been purchased with current taxable income, that it characterizes all secret savings as caches of "hidden treasure" (Br. 36). But experience has shown so many instances of such "hidden treasure" that the probability a given taxpayer did have secret savings is just as fair as

inference as that he did not. In *David Friedberg* v. *United States, supra* No. 18 of this Term, the Government concedes that when the agents made their investigation the taxpayer had in a safe deposit box assets worth $73,225, of which $53,625 was in bonds and $19,600 in currency (see Brief of the United States in Opposition, p. 7). The newspapers often carry news of incidents involving caches of hidden treasure.[12]

The necessity for proving a negative is the result of the Government's own action and not that of the taxpayer. In charging attempted tax evasion, the Government makes the positive assertion that a taxpayer has failed to correctly report his income. Where there is some direct evidence of unreported income, but not in definite amounts, it may use evidence of increase in net worth or expendi-

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[12]New York Times:

March 2, 1952 (p. 33 Col. 2)—L. V. Redfield robbed in Reno, Nevada of an estimated $2,500,000—more than $300,000 in cash.

March 24, 1952 (p. 17 col. 3)—Mrs. Helen M. Bidden, robbed of $125,000 in cash in Reading, Pa., that she had "not gotten around" to banking.

February 8, 1954 (p. 15 col. 7)—86 yr. old woman beaten in attempt to get $500,000 in her safe—$291,800 of it in cash.

March 16, 1954 (p. 30 Col. 3)—Husband absconds with $303,000—$243,500 in cash kept in trunk of new Cadillac.

In cases reported in Tax Court decisions large amounts of cash and securities have in fact been found. In *James Q. Whittemore* v. *Commissioner*, CCH Dec. 16, 700 (M), 7 TCM 845, the revenue agent found in the taxpayer's lock boxes $32,000 in cash, $21,000 in government bonds, and $25,550 in cashiers' checks, a total of $78,550. In *Estate of Maurice J. Lydon* v. *Commissioner*, CCH Dec. 19, 306 (M), 11 TCM 1119, the taxpayer's safe deposit box was found to contain $32,183.25 in cash. In *Maurice A. Spalding* v. *Commissioner*, CCH Dec. 19, 832 (M), 12 TCM 883, the Tax Court sustained a doctor's claim that he had $75,000 in cash at the beginning of the net worth period, and overruled the deficiency as well as the fraud penalty. In *Estate of Halley Tarr* v. *Commissioner*, CCH Dec. 19, 326 (M) 11 TCM 1151, the taxpayer had $39,200 in cash.

tures to "reinforce" the direct proof. *United States* v. *Johnson, supra,* p. 517. But where the Government relies on increases in net worth alone as evidence of taxable income, it assumes all the burdens of so proving. When it asks the jury to infer that the increase was not only from taxable income, but from current income of that particular year, it must offer sufficient evidence to overcome the equally justifiable inference that the increase was from nontaxable sources. By choosing to prosecute cases where it has no direct proof, the Government assumes the burden inherent in circumstantial evidence cases. The *Johnson* case does *not* support the Government's claim that discrepancies between income reported and an increase in net worth (with or without proof of cash on hand) are *alone* substantial evidence supporting an inference that respondent had unreported income.

The Government has succeeded in convincing a few courts to adopt its negative averment theory, and shift to the defendant the burden of proving his innocence. *Jelaza* v. *United States,* 179 F. 2d 202 (C. A. 4); *Bell* v. *United States,* 185 F. 2d 302 (C. A. 4) certiorari denied 340 U. S. 930; *Smith* v. *United States,* 210 F. 2d 496, 500 (C. A. 1), No. 52 of this Term. However, this breach of one of the cardinal rules of criminal law has been deprecated by other courts. In *Demetree* v. *United States, supra,* p. 494, the Fifth Circuit said:

> ". . . Further and more prejudicial to a defendant, there has grown up a kind of ancillary theory that the government, by introducing proof of deposits, expenditures, etc., having put up what it calls a *prima facie* case, the defendant finds himself jockeyed out of the position the law affords him, of insisting that the government establish his guilt by legal and

> credible evidence beyond a reasonable doubt. This is accomplished by requiring him to prove himself innocent by assuming the burden of overcoming the prejudicial effect of the mass of exhibits, estimates, conjectures, and conclusions which the government has been allowed to get into the record, upon the apparent theory that it is up to the defendant to explain all of it away as part of his burden to prove his innocence."

and, *United States* v. *Casserta, supra,* p. 907, the Third Circuit said:

> ". . . The cases show, however, a rather surprising rule that when the discrepancy between increased net worth and reported income is shown the burden of explanation shifts to the taxpayer, at the same time repeating the usual criminal law rule that the burden throughout a criminal case is upon the prosecution."

The unfairness of the Government's contention was pointed out in *United States* v. *Clark,* S. D. Cal. Aug. 4, 1954 unofficially reported 1954 C. C. H. para. 9546, where the court said:

> "* * * What arose out of a special situation in cases where no adequate books have been kept is now so commonly used that there is danger that a prosecution for a serious felony may be based entirely upon disagreement as to bookkeeping methods. And the burden of proof may be shifted entirely on the taxpayer to explain not some items concealed by failure to keep books, but items which books kept in the regular course of business and of the type sanctioned by reputable accountants for a particular business may not reflect."

In spite of the many cases cited by the Government in support of its other points, it does not cite a single one to support its claim that proof of cash on hand is not essential proof of an element of the offense. If the Government's claim were upheld, all it would have to do is have its revenue agents prepare lists of assets owned by taxpayers at the beginning and end of each year. Wherever there was a substantial difference between any increase in the list of assets and the reported income, the difference would be assumed to be current taxable income upon which the taxpayers attempted to evade the tax. It would have the cases go to the jury unless the taxpayers disprove the assumption that the increase represented taxable income.

In requesting this Court to make such a rule, the Department of Justice is seeking to establish for criminal cases less of a burden of proof than the Commissioner of Internal Revenue has been required to bear in sustaining fraud penalties in civil cases in the Tax Court. That court has often upheld the assertion of a deficiency but overruled the fraud penalty on the ground that the Commissioner had not sustained the burden of proof, whereas the presumption in favor of the ordinary deficiency had not been overcome by the taxpayer.[13]

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[13]In *Bonnie G. Gray* v. *Commissioner*, 11 TCM 1213, the Tax Court accepted the Commissioner's contention of omitted income, but held he had not sustained the burden of proof of fraud for the years 1942 and 1944, although the taxpayer had pleaded guilty to income tax evasion for 1943, which year was not before the Tax Court. To the same effect, see *Estate of Maurice J. Lydon* v. *Commissioner*, 11 TCM 1119.

In *A. C. Muldoon* v. *Commissioner*, CCH Dec. 19, 841 (M) 12 TCM 897, the Tax Court said:

> "The respondent determined a fifty per cent addition to tax against each taxpayer for each of the four years. This addition is imposed by section 293 (b) of the Internal Revenue

V.

THE COURT BELOW PROPERLY HELD THAT THE GOVERNMENT HAD NOT PROVEN THE CORPUS DELICTI BY INDEPENDENT EVIDENCE.

The Court below stated that the question for decision was whether respondent's admissions "were properly received in evidence absent any independent evidence of the crime of tax evasion." (R. 218) After considering the record, it held that in the absence of some independent proof of the corpus delicti, respondent's verbal and written extrajudicial admissions were erroneously received in evidence (R. 219).

The Government offered *no evidence at all* to establish by the net worth method the following essential elements of the offense of attempted tax evasion: (1) that respondent's books and records were inadequate to properly reflect his income, (2) that respondent had a source of income not

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Code where any part of the deficiency is due to fraud with intent to evade tax. The burden is upon the respondent to prove fraud. Section 1112, Internal Revenue Code. We do not find affirmative evidence sufficient to sustain this burden. Although we do not accept the taxpayers' story of the vast amount of cash brought to Alaska, and conclude that they have failed to prove that their apparent increase in net worth did not represent unreported income, this negative conclusion is not enough to sustain the additions to tax for fraud. The mere fact of a large understatement of income is not enough. *James Nicholson*, 32 B. T. A. 977 (1935) [Dec. 9024] aff'd 90 Fed. (2d) 978 (C. A. 6, 1937) [37-2 USTC par 9397]. There is no revealed source of the unreported income, nor is there evidence of gambling or other illegal activity of the affirmative nature required to establish fraud. The violation of price ceiling laws indicated by Agent Fleet's report is not sufficient. We are unable to affirm the additions to tax for fraud."

See also *Julius M. Hooper* v. *Commissioner*, CCH Dec. 19, 874 (M) 12 TCM 1017.

disclosed by his books and records and not disclosed on his return, or (3) specific omissions of income from the source disclosed on his books and return, (4) an intent to evade taxes.

The Government offered no *independent* evidence, and relied solely upon respondent's admissions to establish: (5) that he was in any business at all and received any income at all, (6) the cash on hand at the beginning and end of each tax year, (7) that respondent had no other assets on December 31, 1945 than those he allegedly admitted, (8) that respondent had no other non-taxable receipts or income during the tax years involved, such as gifts, inheritances, insurance proceeds, etc.

The Government contends there are two different versions of the rule requiring that a confession must be corroborated by independent evidence of the corpus delicti. It states that the Court of Appeals for the District of Columbia follows the rule that there must be "independent of the confession, substantial evidence of the corpus delicti and the whole thereof". *Forte* v. *United States,* 94 F. 2d 236, 240, affirmed on other issues 302 U. S. 220. However, it contends that the majority of the courts follow the less stringent version of the rule of *Daeche* v. *United States,* 250 Fed. 566, 572 (C. A. 2) that it is unnecessary that the independent evidence alone be sufficient to prove the corpus delicti or that it touch all elements of the corpus delicti (Br. 23-26).

Although the Government erroneously conceived the elements of the corpus delicti of a net worth case, it contends that even under the *Forte* rule, there was corroboration here. However, respondent contends, that when the elements of the corpus delicti in a net worth case are properly conceived, there was no corroboration even under the *Daeche* rule.

The Government questions the wisdom of the rule requiring the same corroboration for extra-judicial admissions as for confessions, but accepts the rule here, and claims the court below erroneously expanded it (Br. 22-23).

It is difficult to understand why the Government went into this discussion about two different rules as to the kind of corroboration needed. There is no question but that the court below followed the rule of the *Daeche* case for which the Government is now contending. The court below, in *Davena* v. *United States*, 198 F. 2d 230, 231, certiorari denied 344 U. S. 878, speaking through Chief Judge Denman, who wrote the opinion in the instant case, stated:

> ". . . in this circuit * * * it is established that the evidence corroborating a confession of the defendant need not independently prove the commission of the crime charged, neither beyond a reasonable doubt nor by the preponderance of proof."

See also *D'Aquino* v. *United States*, 192 F. 2d 338, 357 (C. A. 9).

The only apparent reason why the Government devoted so much of its brief to a discussion of rules (Br. 20-31) which were not questioned by the court below, is a desire to avoid defending its real position. The "Question Presented" in the Government's brief on the merits (Br. 2) is *entirely different from* the "Question Presented" in its petition for a writ of certiorari (Pet. 2). There is a tremendous difference between asking whether a defendant's admissions as to cash on hand "require corroboration", or must be corroborated by "independent evidence of this fact." The court below did NOT hold that any single fact in respondent's extra-judicial admissions must be corroborated by independent evidence of that single fact. It did hold that a mere "list of assets", without any other evidence tending to establish

the commission of the crime of attempted income tax evasion, was not the equivalent of a complete and reasonably accurate "net worth statement", was not material proof of any relevant element of the case, and established no portion of the corpus delicti.

Respondent disagrees with the Government's contention that the court below was concerned only with respondent's alleged admission as to cash on hand, and not with the confession of unreported income in Exhibit 11 (Br. 27, 38). While the court below devoted its main discussion to the admission as to cash on hand, it specifically disagreed with the Government's "claim that Calderon's sworn statement given to the tax officials confessing the under-reporting of his income for the four years" was not an extra-judicial admission (R. 219). It held that neither the verbal nor written statements could be a basis for conviction without independent proof of the corpus delicti (R. 219). Therefore, the issue here is not simply with respect to an admission to a specific fact, but includes an alleged confession of guilt (Br. 27).

The facts to which the liberal rule was applied in *Daeche* indicate independent proof of a nature not found here. There the court found ample corroboration of the existence of an agreement to attack ships, outside of Daeche's confession. He was shown by independent evidence to have been in correspondence with co-conspirators, and to have tried to find means of getting explosives. These facts clearly established one element of the offense—attempting to destroy a vessel—and the confession was received to establish the second element—a conspiracy.

But as has been shown above, the two main elements of this offense are (1) unreported taxable income, and (2) a

willful attempt to evade the tax thereon. There was no evidence at all of the second element, and the Government had only made a beginning at proving the first. The admissions with respect to alleged cash on hand, and the confession in Exhibit 11 will be discussed separately.

The Government could not establish unreported taxable income until it had first accurately established a starting point for the net worth statement. It could not have an accurate starting point until it had accounted for all respondent's assets and liabilities to a reasonable degree of certainty. If the nature of the facts indicated there were assets not "visible" to the revenue agents, such as cash on hand or cash in a safe, the net worth statement could not be complete—and therefore "proves nothing" as the court below held (R. 218)—until those assets are established, or in some way accounted for.

The Government's so-called "independent" evidence established only "subsidiary facts", and was not sufficient to even tend to prove the first element of the offense. It is true that there was uncontroverted evidence of substantial increases in the "visible" assets which the agents saw (Br. 33). The respondent never disputed the fact that he had purchased visible assets during the tax period in question. In fact, he cooperated with the agents during the investigation, and turned over to them all his records (Br. 8-9, R. 87, 88, 140, 172-173). Furthermore, respondent stipulated to all of the assets except "cash on hand" and "cash in bank" (Br. 4, R. 8-9).

The largest increase in any single asset was in the coin-operated machines used in his business. The Government calculated that respondent increased his visible net worth during 1946 by approximately $16,000 in this single asset

(Br. 6-7). But proof of this subsidiary fact does not in any way indicate a real increase in net worth or in taxable income. With respect to this particular asset, respondent testified specifically that the source of funds used to purchase these machines in 1946 was cash he had in his safe at the end of 1945,—or as the accountants state it, on December 31, 1945 (R. 64-66, 164-165). The Government offered no proof whatsoever of the source of any funds used to purchase any of the assets. It considered the $16,000 increase in the asset coin-operated machines income in 1946 solely on the basis that "they popped up" or "came to light" in that year (R. 123).

This illustrates respondent's contention that merely showing an increase in visible assets—as the Government did here—does not tend to prove in fact an increase in net worth, or current taxable income, or an element of the offense of a willful attempt to evade a tax.

The agents arbitrarily selected January 1, 1944 as a starting point. They knew respondent had been in business since 1935 (R. 83), but they made no investigation to determine whether he had accumulated any cash prior to 1944 and relied solely upon his alleged admission. Agent Tucker admitted that he was aware that business was very good in Douglas during the war (R. 83, 91), and knew that respondent had not made any deposits in his savings account from June 1943 to October 1945 (R. 84, 91-92).

The inadequacy of the agents' investigation is evident, and their own testimony establishes it was illogical to interpret any statement respondent may have made during the several interviews as a positive admission that he had on hand *exactly* $500 on December 31st of six successive years. In fact, although Tucker testified respondent told

him he believed he had $500 on hand "on the last day of each year" (R. 59). Tucker also stated he pointed out to respondent he must have had more on December 31, 1949 because he made a cash deposit in his bank account of $1,971.50 on January 4, 1950 (R. 59). It is significant that the agents did *not* accept respondent's statement of $500 cash on hand on December 31, 1949 because it was not to their advantage to do so. Since their investigation disclosed the deposit of $1,971.50 in January 1950, they *put it back* into 1949 in order to *increase* respondent's income for that year. But they made no effort to ascertain whether respondent had more cash at the starting point than the $500 he allegedly admitted, because it was to their advantage to keep that sum low.

If the agents knew anything at all about respondent's business—and they should have learned a great deal if they made a proper investigation—they knew that respondent did have plenty of cash—on December 31st as well as during the year. In fact, agent Tucker admitted that respondent "at times had more cash than that" (R. 85). As far as the record discloses, the only person to whom the agents talked about respondent's business was Verdugo. He told them that respondent "did carry cash, plenty of cash in his safe because of the nature of his business he had to be making change, cashing checks and so forth for his locations" (R. 138).

In the face of these positive facts which demonstrate the unreasonableness and implausibility of the alleged admission, how can the Government's contention be upheld that not one cent of funds on hand December 31, 1945 was used to buy the $16,000 worth of new machines in 1946? They claim he started the year 1946 with exactly $500 in

cash, and ended the year with exactly the same amount. Although respondent was unable to purchase new equipment during the four-year war period, while business was good, the agents claim he had not saved a dollar with which to buy the new equipment he purchased in 1946 (R. 64-65, 91, 164-165). Because they "saw" the equipment in 1946, and did not "see" the cash on December 31, 1945, they charged respondent with the receipt of current taxable income in 1946, even though the resulting net income of $24,855.49 "was out of line" with the figures for the two prior years and two succeeding years (R. 122-123).

The Government contends it offered considerable evidence to negate the possibility that the unexplained increases in net worth could be accounted for by an undiscovered prior accumulation (Br. 34). A careful reading of the record fails to disclose *any evidence at all* offered by the Government on this point. It is necessary to call to this Court's attention an important point of evidence and procedure which should not be overlooked. The Government has made several references in its brief to evidence of facts which it claims *it* proved as part of its case, but which the record shows was not offered by the Government, or was received for an entirely different purpose than is claimed now by the Government.

At the trial the Government proceeded entirely on the theory that a net worth case based upon respondent's alleged admissions and confession was sufficient to convict. It offered no evidence at all about respondent's business or income, made no attempt to describe it, or to show he had income. It based its case upon the stipulation as to assets on hand at the beginning and end of each year plus the signed confession, Exhibit 11. It called only five witnesses, two

bank officers to identify bank records, two employees of the Bureau of Internal Revenue who conducted the investigation of respondent's income tax liability, and Mr. Verdugo, who prepared respondent's income tax returns (R. 31, 34, 40, 50, 127). Verdugo had no independent knowledge of respondent's business, and the only testimony he gave about income was what respondent had told him (R. 129).

After introducing in evidence respondent's income tax returns for the years 1946 to 1949, and some bank records, the Government started immediately to offer proof of net worth (R. 50). With no other evidence at all in the record, the Government offered evidence of respondent's alleged admission as to cash on hand (R. 51). Respondent objected at the outset to any evidence with respect to his admissions on the ground that no proper foundation had been laid, and that the corpus delicti had not been proven (R. 54, 56, 57). Respondent pointed out to the trial court that this point was crucial to the case, and requested an opportunity to cross-examine the witness on voir dire, which was not granted (R. 62-63). Respondent repeated his objection throughout the presentation of the Government's case (R. 68, 98, 100, 107) and at the close of the Government's case moved for a dismissal of the indictment and an acquittal on the specific ground that the corpus delicti had not been proven (R. 141). The description of respondent's background and financial circumstances on pages 4-6 and 34-35 of the Government's brief are based almost entirely on the respondent's testimony. It was not evidence offered by the Government as independent proof of the corpus delicti.

The Government also claims it offered proof of respondent's income tax returns for the years 1941 to 1945 to demonstrate that he had a modest income during that period (Br. 34-35). It cited no page reference to the

record to support its statement, and the record does not support it. At page 6 of its brief, the Government refers to Exhibits 12 and 13, respondent's income tax returns for 1944 and 1945. The record discloses that these exhibits were not offered by the Government as part of its case, and were not offered as affirmative proof to establish lack of prior accumulated funds. They were offered in evidence solely to *impeach* respondent's credibility, and the trial court limited their receipt to that single purpose (R. 183-186).

On page 6 of its brief the Government also refers to income tax returns for the years 1941 and 1942. The record page cited, page 81, does not mention any such returns, nor are they referred to anywhere else in the record. They may be mentioned in defendant's Exhibit A, which is not before this Court, but even if they are, this exhibit was not offered by the Government, but was received in evidence over its objection and used by respondent solely to impeach the credibility and accuracy of the Government agent who was testifying about respondent's alleged admissions with respect to cash on hand (R. 81-82). Offered in this form, it would not have been competent evidence for the Government. Furthermore, there is no showing that the court or jury ever saw the exhibit.

It is clear, therefore, that none of the defendant's testimony on cross-examination may be used as affirmative proof by the Government. See *United States* v. *Waldon*, 114 F. 2d 982, (C. A. 7) certiorari denied 312 U. S. 681.

In its petition for a writ of certiorari the Government raised only one objection to the opinion of the court below—the ruling with respect to the net worth starting point. Its brief in this court indicates that it considers that the only point decided (Br. 27). It is difficult to understand how

the Government reached this conclusion, as the alleged confession contained in Exhibit 11, if properly admitted, would have been sufficient so sustain a conviction under the arguments now presented by the Government, even if there had been no admissions as to cash on hand.

Respondent objected to the admission of Exhibit 11 on the same grounds as the other statements, viz. that the Government had not first established the corpus delicti by independent evidence (R. 107). The point was argued at length in his brief in the court below (Brief of Appellant in the Court of Appeals, pp. 4, 5, 6, 18-20). The court below considered this sworn statement an extra-judicial statement, and subject to the same requirement of corroboration as the other admissions (R. 219). As has already been amply demonstrated, there was no independent evidence that any income had in fact been omitted from the returns. The Government relied entirely upon proof of increases in net worth to justify its claim that there were unreported receipts. When the court below held the properly admitted evidence as to net worth was not sufficient to satisfy the minimum requirements of proof of the corpus delicti, it followed that Exhibit 11 was likewise inadmissible.

There can be no doubt that the Government is attempting to persuade this court to ease its burden of proof in criminal tax cases based upon the net worth method. It is not satisfied with the long record of convictions affirmed by the Ninth Circuit in tax cases involving proof by the net worth method. See, *Barcott* v. *United States,* 169 F. 2d 929 (C. A. 9), *Gendleman* v. *United States,* 191 F. 2d 993 (C. A. 9), *Davena* v. *United States,* 198 F. 2d 230 (C. A. 9), *Goldbaum* v. *United States,* 204 F. 2d 74 (C. A. 9),

Remmer v. *United States,* 205 F. 2d 277 (C. A. 9), *McFee* v. *United States,* 206 F. 2d 872 (C. A. 9), and others.

In all these cases, as well as the instant case, the Ninth Circuit followed the rule: "The fundamental question presented is what quantum of evidence must be offered by the Government before a trial court can properly submit the case to the jury." *Remmer* v. *United States, supra,* p. 280. In all the cases cited it held there was sufficient evidence to go to the jury. But when the instant case came up, with no independent evidence at all, it properly held that the Government could not short-cut taxpayers into jail. The law and the Constitution put the burden on the Government to prove guilt beyond a reasonable doubt. The instant decision means no more than that the internal revenue agents must do a thorough job of investigation, which was not done here.

The Ninth Circuit did not need to write a long opinion to explain to the Government all the things which were lacking in this case. It quickly pointed out at the beginning that respondent operated "a *legitimate* coin-machine business" (italics supplied) (R. 218). It was not dealing with a racketeer, or a clever, skillful, big-time gambler, or with huge sums of money and extravagant expenditures. What was presented was a "little fellow" with a good reputation for honesty among responsible citizens in the community, and a case so weak the Government had to try him twice in order to obtain a conviction (R. 86, 219). The court below had substained many convictions for the Government, but when the Government failed to present sufficient evidence that a crime was committed, it refused to permit it to stand, as it had previously done in *Spriggs* v. *United States,* 198 F. 2d 782 (C. A. 9).

In other cases the courts of appeals have upheld convictions where they felt the agents did make a thorough

investigation and produced a sufficient quantum of proof to fulfill the Government's burden. In *Remmer* v. *United States, supra,* p. 287, the court said: "In the instant case the Government thoroughly investigated appellant's potential sources of net worth." In *Pollock* v. *United States,* 202 F. 2d 281, 284, (C. A. 5) certiorari denied 345 U. S. 993, the court said: "In the present case the Government agents made a rather thorough independent investigation." In *McFee* v. *United States, supra,* p. 874, the court said: "In a net worth case the Government must establish with a reasonable degree of accuracy the taxpayer's net worth at the beginning and end of the period in question. We think the requirement was fully and adequately met in this case." In *Chapman* v. *United States,* 168 F. 2d 997, 1001 (C. A. 7) certiorari denied 335 U. S. 853, relied upon by the court below in reversing the conviction, the Seventh Circuit stated that: "In a 'net worth case' the starting point must be based upon a solid foundation and a Revenue Agent's statement of the defendant's oral admission or confession when uncorroborated is not sufficient to convict." It affirmed the conviction there because it found the necessary corroboration.

As the Ninth Circuit stated in *Spriggs* v. *United States, supra,* it is not important whether the statement is labeled an admission or confession—under any name there must be independent proof of a crime having been committed before a conviction can be sustained. Furthermore, since cash on hand is an essential item in establishing net worth, and the net worth statement was the only evidence offered to prove both elements of the offense, (1) unreported taxable income and (2) intent to evade the tax thereon, the admission was of as great importance to a conviction as a confession of the

whole offense. The following quotation in *Gulotta* v. *United States*, 113 F. 2d 683, 686 (C. A. 8) is pertinent:

> "Indeed, there is no sound reason why an uncorroborated voluntary admission of some element of crime should be given greater force as evidence of guilt than is accorded the accused's outright confession of the crime itself."

VI.

THERE WAS NO EVIDENCE OF WILLFULNESS

Although the Government agrees that there are two elements to this offense (1) unreported taxable income and (2) a willful attempt to evade the tax thereon, there is no discussion of the second element at all in its brief. Even if a jury may be permitted to assume that a mere showing by the Government of an increase in visible net worth is evidence of *current* taxable income, without independent proof of cash on hand at the starting point, and without proof negativing the possibility that the increases were due to other non-taxable receipts, there is no justification for inferring a willful intent to evade the tax. In the instant case there was no evidence at all of conduct from which a jury could find the affirmative action or concealment indicated in *Spies* v. *United States*, 317 U. S. 492, 499, as necessary to establish the element of willful attempt to evade. The record is barren of any evidence which could be called indicia of fraud. A "bare" net worth case in which the Government simply lists assets and shows an annual increase beyond the reported income lacks an essential element of proof. There must be something additional, such as failure to keep records of income, false entries in books, concealing

sources of income, concealing ownership of assets by use of dummies or relatives, attempts to bribe, etc.

Respondent's income tax returns were based upon his books, in accordance with a method of accounting which the investigating agent considered adequate (R. 89). Even if the Commissioner has authority to set up a tax on a different accounting basis for purposes of collection, there is no justification for finding a taxpayer guilty of attempting to evade such tax in a criminal case. The unfairness of such a result is aptly illustrated in the instant case. The Government agent admitted that the net income based upon the net worth statement, showing approximately $24,000 net income for 1946 "was out of line" with the figures of $8,000 for 1944, $8,000 for 1945, $11,000 for 1947 and $6,700 for 1948 (based upon the same net worth statement). He justified the assertion of the deficiencies solely on the ground that the assets "came to light" in those years (R. 123). Yet the uncontradicted evidence was that the Air Base closed down at the beginning of 1946, and business declined (R. 47, 180-181). It is unreasonable to conclude that business was much better in 1946 after the Air Base was closed, than it was during the war years.

A case predicated solely upon increases in net worth is entirely void of evidence from which a jury might infer intent to evade a tax. No evidence at all was presented from which any such inference could be drawn. On the contrary, the record discloses that respondent cooperated fully with the agents in their effort to determine his correct tax liability (R. 87, 88, 140, 172-173). He was not in an illicit business, and did not conceal either his business or his income. His returns disclosed his sources of income, and the Government does not claim he had any others. While

character evidence is not ordinarily of much weight on appeal, nevertheless, the fact that he was so well-known in the community that he was able to obtain as witnesses the Mayor (R. 147), Chief of Police (R. 149), a member of the Arizona State legislature (R. 143), and a former Deputy Collector of Internal Revenue (R. 150), demonstrates that it was unnecessary for him to hide his business or income. They all vouched for respondent's honesty and truthfulness. Since all the machines were operated openly and legally the means was available to the agents to check respondent's receipts from direct sources if they were interested.

The Government offered no evidence at all with respect to the element of intent. The only evidence in the record on this issue is Verdugo's testimony that he told the agents that in his own mind he was sure respondent never intended to defraud anybody (R. 141). There was evidence that respondent was thrifty and industrious, but none that he was dishonest (R. 143-151). Due to his lack of education and dependence upon others (R. 134, 138, 141, 151-152), his income may not have been correctly reported, but there was no evidence of fraud.

There is completely lacking proof of willful intent required by *Spies* v. *United States supra*, *United States* v. *Murdock*, 290 U. S. 389, and *Lurding* v. *United States*, 179 F. 2d 419, 422 (C. A. 6).

This is a "bare" net worth case. It represents an effort by the Government to extend the scope of prosecutions for attempted income tax evasion to new frontiers. In its zeal to enforce the revenue laws the Government is encroaching upon basic constitutional rights of citizens, and violating established principles of criminal law. Apparently what the

Government is now seeking is a special set of rules of criminal evidence and law to be applied to income tax prosecutions alone so that the prima facie correctness of the determination of the Commissioner of Internal Revenue will be sufficient to require a given defendant to prove his innocence. It is attempting to extend to criminal cases the special rule of ordinary civil cases (not involving fraud), which shifts the burden of proof to the taxpayer.[14]

The court below, which has sustained many convictions based upon the net worth method, recognized that there was danger of violation of defendants' constitutional rights in the Government's unbridled use of the net worth method of computing income. Millions of taxpayers file returns every year, and thousands are later found to have underpaid their taxes. But only where the understatement was with intent to evade the tax is a crime committed. The crux of the offense is willfulness. The Government must prove by direct proof or circumstances that a taxpayer knew or should have known his return was false. "There is no presumption that may be drawn from the act itself (filing an inaccurate return)—both knowledge and willfulness must be established by independent proof, direct or circumstantial." *Lurding* v. *United States supra* p. 422. "A willful evasion of the tax requires an intentional act or omission" and "a conviction cannot be sustained unless this state of mind is supported by the evidence" *United States* v. *Martell*, 199 F. 2d 670, 672 (C. A. 3).

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[14]The Government contends for a less burden of proof of the element of intent in criminal cases than the Commissioner of Internal Revenue is required by the Tax Court to sustain with respect to civil fraud penalties. See cases cited at footnotes 12 and 13. See also *King Tsak Kwong* v. *Commissioner*, CCH Dec. 19, 924 (M) 12 TCM 1136.

This Court has carefully considered the relation of this offense to other penalties imposed by Congress to enforce the tax laws. *Spies* v. *United States supra*. Congress has provided three separate and distinct methods and procedures for enforcing the revenue laws: (1) a civil proceeding in which the Commissioner's determination of a deficiency is prima facie evidence that a tax is due; (2) a civil proceeding in which the Commissioner asserts a 50 per cent penalty for fraud and *the Commissioner has the burden* of proving fraud by clear and convincing evidence; (3) a criminal proceeding, which is available when the case warrants punishment in addition to the 50 per cent penalty, and where the Government has the burden of proving beyond a reasonable doubt every element of the offense, including a tax liability.

> "The climax of this variety of sanctions is the serious and inclusive felony defined to consist of willful attempt in any manner to evade or defeat a tax" * * *
>
> "But in view of our traditional aversion to imprisonment for debt, we would not without the clearest manifestation of congressional intent assume that mere knowing and intentional default in payment of a tax, where there had been no willful failure to disclose the liability, is intended to constitute a criminal offense of any degree. We would expect willfulness to include some element of evil motive and want of justification in view of all the financial circumstances of the taxpayer". *Spies* v. *United States, supra*, p. 497.
>
> "We think that in employing the terminology of attempt to embrace the gravest of offenses against the revenues, Congress intended some willful *commission* in addition to the willful omissions that make up the list of misdemeanors". (italics supplied) id. p. 499.

Under this test mere proof of increases in net worth, without other evidence of affirmative acts, is insufficient to establish the criminal intent required by the statute.

VII.

THE DECISION OF THE COURT BELOW REVERSING THE CONVICTION WAS CORRECT.

The court below did not engraft an extension upon the corroboration rule as contended by the Government (Br. 12, 14, 19). It did apply fundamental principles of criminal law. As this Court said in *Brinegar* v. *United States*, 338 U. S. 160, 174:

> "Guilt in a criminal case must be proved beyond a reasonable doubt and by evidence confined to that which long experience in the common-law tradition, to some extent embodied in the Constitution, has crystallized into rules of evidence consistent with that standard. These rules are historically grounded rights of our system, developed to safeguard men from dubious and unjust convictions, with resulting forfeitures of life, liberty and property."

The decision below is in accord with the principle that where the prosecution relies upon circumstantial evidence, the evidence must exclude every reasonable hypothesis other than the guilt of the defendant. *Bryan* v. *United States*, *supra*, p. 227; *United States* v. *Fenwick*, *supra* p. 492; *Hanson* v. *United States*, 208 F. 2d 914, 916 (C. A. 6).

Since almost every adult in the United States is subject to the income tax laws, almost every adult in the country is a possible suspect. Perhaps no other Federal offense has such a wide field in which it may occur. The number of

persons who may be involved in offenses involving contraband, such as counterfeiting or narcotics, is a comparatively small percentage of the population. In view of the fact that almost everyone is liable to the income tax law, and since the determination of the correct tax liability is very often a difficult problem involving honest disagreement between taxpayers and the Commissioner of Internal Revenue, criminal penalties should be imposed only in the clearest cases. Where the Government offers definite proof of specific income omitted, or false deductions claimed, the intent to evade may be clear. But when the Government uses a theory to attempt to reconstruct income or assume that there must have been income, there is cause for grave concern as to the wisdom of such a policy. There is serious doubt that a net worth computation has sufficient reliability as proof of current taxable income that its use should be permitted at all in a criminal case. But if it is to be permitted, certainly there should be definite standards which should be met as prerequisites requiring the Government to establish guilt beyond a reasonable doubt with evidence of demonstrated probative value.

The court below correctly ruled that it was error to have admitted in evidence the oral and written admissions made to the agents. Without the alleged oral admissions with respect to cash on hand there was no complete net worth statement, and without the written statement, Exhibit 11, there was no other evidence of unreported income.

In holding that the record lacked independent evidence of the corpus delicti the court below followed a long line of its own decisions as well as other courts of appeals (see pp. 58-60 *supra*). It is the Government which now seeks a new rule, to enable it to obtain convictions without afford-

ing taxpayers the fundamental rights granted to defendants in all other kinds of criminal cases. The proper enforcement of the internal revenue laws does not require that the Government be granted the same privileges as to burden of proof in criminal cases as it enjoys in ordinary civil cases in the Tax Court.

From the holding that there was no independent evidence of the corpus delicti, it necessarily follows that the Government failed to prove a prima facie case. Accordingly, the motion for acquittal should also have been granted. Having tried respondent twice, and the record clearly demonstrating that the Government does not possess sufficient legal evidence to convict him, it is not in the interests of fairness and justice to award the Government a third try.

CONCLUSION

It is respectfully submitted that the judgment of the court below reversing and remanding should be modified by an instruction to reverse and enter a judgment of acquittal.

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